

The FOMC in 1982: De-emphasizing M1

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THE year 1982 was marked by rapid and variable growth of the monetary aggregates. The growth of M1, the narrow monetary aggregate, was up sharply from 1981, while M2 growth was slightly above the previous year's rate. Of the three targeted aggregates, only M3 growth was lower in 1982 than in 1981. Moreover, 1982 marked the first time since the Federal Open Market Committee (hereafter FOMC or Committee) adopted its new procedures in October 1979 that the fourth-quarter-to-fourth-quarter growth rate of M1 accelerated.¹

As was the case in 1981, the Committee faced unusual uncertainties regarding the relative behavior of M1 and M2 during the year associated with various technical factors, regulatory changes and financial innovations. Furthermore, the income velocities of the monetary aggregates, especially that of M1, declined relative to their historical norms.² Because of these difficulties, the Committee had considerable discussion about the weight that should be assigned to M1

and M2 as a guide to policy. Ultimately, it decided to suspend setting explicit growth objectives for M1 during the fourth quarter of the year. This article will review the factors affecting the long- and short-run policy decisions of the Committee during 1982, including those leading up to the decision to suspend setting an explicit target for M1.

ANNUAL TARGETS FOR 1982

The Full Employment and Balanced Growth Act of 1978 (the Humphrey-Hawkins Act) requires the Board of Governors to transmit to Congress, each February and July, reports on the objectives for growth rate ranges for monetary and credit aggregates over the current calendar year and, in the case of the July report, over the following calendar year as well.³ The Committee has chosen to establish ranges from the fourth quarter of the previous year to the fourth quarter of the current year.⁴

Note: Citations referred to as "Record" are to the "Record of Policy Actions of the Federal Open Market Committee" found in various issues of the *Federal Reserve Bulletin*.

¹For a description of the operating procedure, see R. Alton Gilbert and Michael Trebing, "The FOMC in 1980: A Year of Reserve Targeting," this *Review* (August/September 1981), pp. 2-22; and Richard W. Lang, "The FOMC in 1979: Introducing Reserve Targeting," this *Review* (March 1980), pp. 2-25.

²The income velocity of a monetary aggregate is given by the ratio of nominal GNP to the aggregate. It indicates the number of times each unit of nominal money "turns over" in producing this year's final output. This conclusion about the record decline in velocity was based on the fact that M1 growth had been rapid in the first quarter compared with what would have been predicted on the basis of the actual behavior of nominal GNP and interest rates. This interpretation was supported by the growth in relatively low-interest-yielding savings deposits. See "Record" (June 1982), pp. 366-67.

³These ranges must be reported to Congress each February and July, although the Act provides that the Board and the Committee may reconsider the annual ranges at any time. The period to which the annual ranges apply, however, may not be changed. The base period that the Committee has chosen (the fourth quarter of the previous year) would remain the same even if the Committee decided to change the desired growth rates of the aggregates for the year.

⁴Before 1979, the Committee adopted one-year growth rates each quarter, and the base period for the annual targets announced each quarter was brought forward to the most recent quarter. This method resulted in a problem referred to as "base drift." Growth in aggregates above (below) an annual growth range in a quarter would raise (lower) the base level for calculating the next annual growth path. The specification of annual objectives in terms of calendar year growth rates, which eliminates the base drift problem within a calendar year, does not solve this problem from one calendar year to the next, since new ranges are established from the end of each calendar year.

Organization of the Committee in 1982

The Federal Open Market Committee (FOMC) consists of 12 members: the seven members of the Federal Reserve Board of Governors and five of the 12 Federal Reserve Bank presidents. The Chairman of the Board of Governors is, by tradition, also chairman of the Committee. The president of the New York Federal Reserve Bank is, also by tradition, its vice chairman. All Federal Reserve Bank presidents attend Committee meetings and present their views, but only those presidents who are members of the Committee may cast votes. Four memberships rotate among Bank presidents and are held for one-year terms beginning March 1 of each year. The president of the New York Federal Reserve Bank is a permanent voting member of the Committee.

Members of the Board of Governors at the beginning of 1982 included Chairman Paul A. Volcker, Preston Martin, Henry C. Wallich, J. Charles Partee, Nancy H. Teeters, Emmett J. Rice and Lyle E. Gramley.¹ The following presidents served on the Committee during January and February 1982: Anthony M. Solomon (New York), Edward G. Boehne (Philadelphia), Robert H. Boykin (Dallas), E. Gerald Corrigan (Minneapolis) and Silas Keehn (Chicago). The Committee was reorganized in March and the four rotating positions were filled by: John J. Balles (San Francisco), Robert P. Black (Richmond), William F. Ford (Atlanta) and Karen Horn (Cleveland).²

The Committee met eight times during 1982 to discuss, among other things, economic trends and to decide upon the future course of open market operations.³ As in previous years, however, telephone or telegram consultations were held occasionally between scheduled meetings. During each regularly scheduled meeting, a directive was issued to the Federal Reserve Bank of New York. Each directive contained a short review of economic developments, the general economic goals sought by the Committee, and instructions to the Manager of the System Open Market Account at the New York Bank for the conduct of open market operations. These instructions were stated in terms of short-term rates of growth of M1 and M2 that were considered to be consistent with desired longer-run growth rates of the monetary aggregates.⁴ The Committee also specified intermeeting ranges for the federal funds rate. These ranges provide a mechanism for initiating consultations between meetings whenever it appears that the constraint on the federal

funds rate is proving inconsistent with the objectives for the behavior of the monetary aggregates.

The Account Manager has the major responsibility for formulating plans regarding the timing, types and amount of daily buying and selling of securities in fulfilling the Committee's directive. Each morning the Manager and his staff plan the open market operations for that day. This plan is developed on the basis of the Committee's directive and the latest developments affecting money and credit market conditions, growth of the monetary aggregates and bank reserve conditions. The Manager then informs staff members of the Board of Governors and one voting president about present market conditions and open market operations that he proposes to execute that day. Other members of the Committee are informed of the daily plan by wire.

The directives issued by the Committee and a summary of the reasons for the Committee actions are published in the "Record of Policy Actions of the Federal Open Market Committee." The "Record" for each meeting is released a few days after the following Committee meeting. Soon after its release, the "Record" appears in the Federal Reserve Bulletin. In addition, "Records" for the entire year are published in the Annual Report of the Board of Governors. The "Record" for each meeting during 1982 included:

- 1) A staff summary of recent economic developments — such as changes in prices, employment, industrial production and components of the national income accounts — and projections of general price, output and employment developments for the year ahead;
- 2) A summary of recent international financial developments and the U.S. foreign trade balance;
- 3) A summary of recent credit market conditions and recent interest rate movements;
- 4) A summary of open market operations, growth of monetary aggregates and bank reserves, and money market conditions since the previous meeting;
- 5) A summary of the Committee's discussion of current and prospective economic and financial conditions and the current policy considerations, including money market conditions and the movement of monetary aggregates;
- 6) Conclusions of the Committee;
- 7) A policy directive issued by the Committee to the Federal Reserve Bank of New York;
- 8) A list of the members' voting positions and any dissenting comments;
- 9) A description of any actions and consultations that may have occurred between the regularly scheduled meetings.

¹Governor Frederick H. Schultz's term expired January 1982. He was replaced by Preston Martin.

²Karen Horn took office as President of the Cleveland Bank May 1, 1982, and subsequently became a voting member of the FOMC. Mr. Winn voted as an alternate member in March.

³No formal meetings were held in January, April, June or September of 1982.

⁴In October 1982, short-run objectives for M1 were dropped and short-run objectives for M3 were adopted.

Table 1
FOMC Operating Ranges — 1982

Short-Run Operating Ranges					
Date of meeting	Federal funds rate range	Periods to which monetary growth paths apply	M1	M2	M3
February 1–2, 1982	12–16%	January–March	no further growth ¹	around 8%	no range set
March 29–30 ^a	no change	March–June	about 3%	about 8%	no range set
May 18 ^b	10–15%	March–June	reaffirmed targets		
June 30–July 1 ^c	no change	June–September	about 5%	about 9%	no range set
August 24 ^d	7–11%	June–September	reaffirmed targets		
October 5 ^e	7–10½%	September–December	no specific objective	around 8½–9½%	around 8½–9½%
November 16 ^f	6–10%	September–December	no specific objective	around 9½%	around 9½%
December 20–21 ^g	no change	December–March	no specific objective	around 9½%	about 8%
Long-Run Operating Ranges					
Date of meeting	Target Period	M1	M2	M3	
February 1–2, 1982 ^h	IV/81–IV/82	2½–5½%	6–9%	6½–9½%	
July 15 (telephone meeting) ⁱ	IV/81–IV/82	reaffirmed above range	reaffirmed above range	reaffirmed above range	

¹At its December 1981 meeting the Committee set an objective for M1 of “around 4 to 5 percent,” however, the surge in M1 growth in January prompted the Committee to set a “no further growth” objective at its February meeting.

At its February meeting, the Committee completed the review, begun at its December 1981 meeting, of the annual targets for the monetary and credit aggregates for 1982. It remained committed to its long-standing goal of restraining the growth of money and credit to reduce further the rate of inflation. Nevertheless, Committee members disagreed about the precise ranges to set for the various monetary aggregates. Most members favored reaffirming the ranges for M1 that had been tentatively adopted at the July 1981 meeting. A substantial number, however, favored a somewhat higher range for M2 based on the belief that various developments during the year would likely boost the growth of M2 relative to M1.⁵ Also, it was generally agreed to give considerable weight to M2 in interpreting developments during the year.⁶

In setting its growth range for M1, the Committee argued that the growth in “other checkable deposits,” which had accelerated during January and which was in large part responsible for the rapid January growth of M1, was likely to be temporary, and that the relationship between the M1 growth and the nominal GNP growth likely would be closer to its historical pattern during 1982. On this assumption, the Committee argued that it would be acceptable for M1 to grow at a rate near the upper end of its annual range during 1982. The Committee also expected that the growth of M2 would be high in its range, although somewhat below that of 1981.⁷ At the end of the discussion, the Committee reaffirmed its tentative ranges for M1 and M2. These ranges are presented in table 1.

⁵At its midyear review of the annual ranges, the Committee establishes tentative ranges for the monetary aggregates for the next year — measured from the fourth quarter of the current year to the fourth quarter of the following year.

⁶See “Record” (April 1982), pp. 232–33.

⁷Indeed, the Committee believed that the growth in M2 might meet or exceed the upper end of its range if the personal savings rate grew more rapidly than anticipated, or if depository institutions attracted an exceptionally large flow of funds into IRAs from sources outside of M2. See “Record” (April 1982), p. 233.

Table 1 (continued)

Footnotes — Dissents to FOMC Actions

^aMessrs. Black and Wallich dissented from this action because they favored specification of somewhat lower rates for monetary growth from March to June than those adopted by the Committee, which would be associated with a relatively prompt return of M1 growth to its range for the year.

Mr. Black believed that continued growth of M1 above its longer-run range for any extended period would adversely affect economic activity by exacerbating inflationary expectations and weakening markets for longer-term securities; for that reason, he felt that it was particularly important to resist any surge in growth of M1 that might develop in April.

In Mr. Wallich's opinion, it would be desirable to restrain the pace of prospective recovery in economic activity consistent with some reduction in the unemployment rate to sustain a degree of pressure for the continuation of the reduction in the underlying rate of inflation.

^bMrs. Teeters dissented from this action because she favored specification of somewhat higher rates of monetary growth from March to June with the objective of improving liquidity and easing financial pressures. In her opinion, the time had come to foster lower and less variable interest rates in order to enhance prospects for significant recovery in output and employment.

^cMessrs. Black, Ford and Wallich dissented from this action because they favored a policy for the period immediately ahead that was firmly directed toward bringing the growth of M1 down to its range for 1982 by the end of the year. They were concerned that accommodation of relatively rapid growth over the summer months might jeopardize achievement of the monetary objectives for the year and thus would risk exacerbating inflationary expectations. Accordingly, they believed that tendencies toward rapid monetary expansion in the months immediately ahead should be met by greater pressures on bank reserve positions and in the money market.

Mrs. Teeters dissented from this action because she favored specification of somewhat higher rates for monetary growth during the third quarter along with an approach to operations early in the period that would clearly signal an easing in policy. In her opinion, policy at this point should be directed toward exerting downward pressure on short-term interest rates in order to promote recovery in output and employment.

^dMr. Wallich dissented from this action because he favored an approach to operations early in the period that would lessen the chances of short-term interest rates remaining below the prevailing discount rate or falling further below it. He was concerned that such interest rate behavior would tend to accelerate monetary expansion and that the necessary restraint of reserve growth to curb such expansion might lead to a sizable rebound in short-term rates with adverse implications for business and consumer confidence.

^eMr. Black dissented from this action because he preferred to direct operations in the period immediately ahead toward restraining monetary growth. Although he was mindful of the current difficulties of interpreting the behavior of M1, he was concerned that the recent strength in M1 might be followed by still more rapid growth in lagged response to the substantial decline in short-term interest rates that had occurred in the summer, which could require even more restrictive operations later.

Mr. Ford dissented from this action because he preferred a policy for the period immediately ahead that was more firmly directed toward restraining monetary growth, although he recognized that the behavior of M1 in particular would be difficult to interpret. He was concerned that the Committee's policy directive might be misinterpreted in ways that could adversely affect pursuit of the System's longer-run anti-inflationary objectives, particularly in the context of a highly expansive fiscal policy program.

Mrs. Horn dissented from this action because she preferred to continue setting a specific objective for growth of M1, as well as for M2, over the current quarter, notwithstanding the problems of interpreting its behavior. In setting a target for M1, she would tolerate faster growth early in the period, owing to the uncertain impact of the proceeds from maturing all-savers certificates, and would give greater weight to the behavior of M2 for some weeks after the introduction of the new instrument at depository institutions.

^fMr. Ford dissented from this action because he believed that it ran the risk of complementing very large budget deficits with substantial increases in the supply of money. In his view, the result would be an overly stimulative combination of policies that could rekindle inflation and drive up interest rates during 1983.

^gMr. Black dissented because he preferred to direct policy in the weeks immediately ahead toward ensuring that the growth of M1, abstracting from temporary effects of the introduction of new money market deposit accounts, would moderate from the extremely rapid rate of recent months. While recognizing the difficulties in interpreting M1 currently, he was concerned that excessive underlying growth in that aggregate might reverse the progress achieved in reducing inflation and inflationary expectations and lead to substantially weaker markets for long-term securities.

Mr. Ford dissented from this action because he continued to prefer a policy for the current period that was more firmly directed toward restraining monetary growth, after allowance for the short-run impact of the introduction of new money market deposit accounts. He remained concerned that rapid expansion in the supply of money together with very large budget deficits would produce an overly stimulative combination of policies that could rekindle inflation and inflationary expectations and lead to higher interest rates during 1983 and 1984.

^hMrs. Teeters dissented from this action because she believed that somewhat higher monetary growth over the year ahead was needed to promote adequate expansion in economic activity and a reduction in the rate of unemployment. Specifically, she favored a range for M1 that was at least $\frac{1}{2}$ percentage point higher than that adopted by the Committee and a range for M2 that provided for somewhat greater growth in the broader aggregate relative to that in M1.

ⁱMrs. Teeters dissented from this action because she favored an explicit statement that growth of M1 above the upper end of the Committee's range for 1982 by 1 percentage point, or even as much as $1\frac{1}{2}$ percentage points, might be acceptable. In her opinion, it was important to indicate the acceptable degree of growth of M1 above the range in order to foster market behavior that would lower interest rates and enhance the prospects for sustaining recovery in output and employment.

Table 2

Planned Growth of Monetary Aggregates for 1982
(percentage changes, fourth-quarter-to-fourth-quarter)

Aggregate ¹	Actual 1981 growth rate ²	Proposed range for 1982	Actual 1982 growth rate ²
M1	5.0%	2.5-5.5%	8.5%
M2	9.5	6.0-9.0	9.9
M3	11.4	6.5-9.5	10.4

¹M1 is defined as currency plus private demand deposits and other checkable deposits at depository institutions exclusive of deposits due to foreign commercial banks and official institutions, plus travelers checks of non-bank issuers.

M2 is M1 plus savings and small-denomination time deposits at all depository institutions, shares in money market mutual funds, overnight repurchase agreements issued by commercial banks and overnight Eurodollar deposits held by U.S. residents at Caribbean branches of U.S. banks.

M3 is M2 plus large time deposits at all depository institutions and term repurchase agreements issued by commercial banks and savings and loan associations.

²Data as revised by Board of Governors in January 1983.

Actual Money Growth in 1982

As shown in table 2, all three of the monetary aggregates exceeded their target ranges during 1982.⁸ Their patterns of growth relative to their ranges, however, were considerably different, as can be seen in chart 1. Both M1 and M2 were above their targeted ranges nearly all of the year. In contrast, M3 growth was within its range during the first half of 1982 and above it during the second half.

Although both M1 and M2 were above their target ranges throughout the year, their growth rates displayed different patterns. While the quarter-to-quarter growth of M2 during 1982 was less stable than that of 1981, it was stable compared with the quarter-to-quarter growth of M1. M1 grew rapidly in January and was fairly flat until July, when it began a growth spurt that accelerated markedly in October. This pattern of M1 growth was basically consistent with the Committee's short-run objectives for the year.

SHORT-RUN POLICY DIRECTIVES FOR 1982

The announced annual target ranges for the monetary aggregates provide a basis on which the FOMC

chooses its short-run policy objectives during the year. The short-run policy directives, however, are the ones that influence the *day-to-day* implementation of monetary policy. The Committee issues these directives for implementation by the Manager of the Open Market Account at the Federal Reserve Bank of New York.

During 1982, the Committee specified short-run growth rates for M1, M2 and M3.⁹ It also specified intermeeting ranges for the federal funds rate as a mechanism for initiating further consultations in periods between regularly scheduled meetings.¹⁰ These intermeeting ranges and the actual federal funds rate are presented in chart 2. The growth rate targets for the monetary aggregates and the intermeeting ranges for the federal funds rate that the Committee specified during 1982 appear in table 1.

As in the previous year, discussions pertaining to short-run policy decisions in 1982 were marked by considerable uncertainty about both the effect of various regulatory changes and financial innovations on the growth rates of the monetary aggregates and the

⁸The definition of M2 was changed effective February 14, 1983, to include tax-exempt money market funds and to exclude all IRA/Keogh balances at depository institutions and money market mutual funds. These changes also affected M3. Thus, data available January 20, 1983, were used. The growth rates of M1, M2 and M3 will differ from those reported from revisions after February 14, 1983.

⁹The short-run growth rate target for M1 was dropped at the October meeting and a short-run target for M3 was introduced.

¹⁰If movements of the federal funds rate within the range appear to be inconsistent with the short-run objectives for the monetary aggregates and related reserve paths during the intermeeting period, the Manager of Domestic Operations at the Federal Reserve Bank of New York is to notify the Chairman, who in turn decides whether the situation calls for supplementary instructions from the Committee.

Chart 1

Long-Run Operating Ranges for the Period IV/81-IV/82

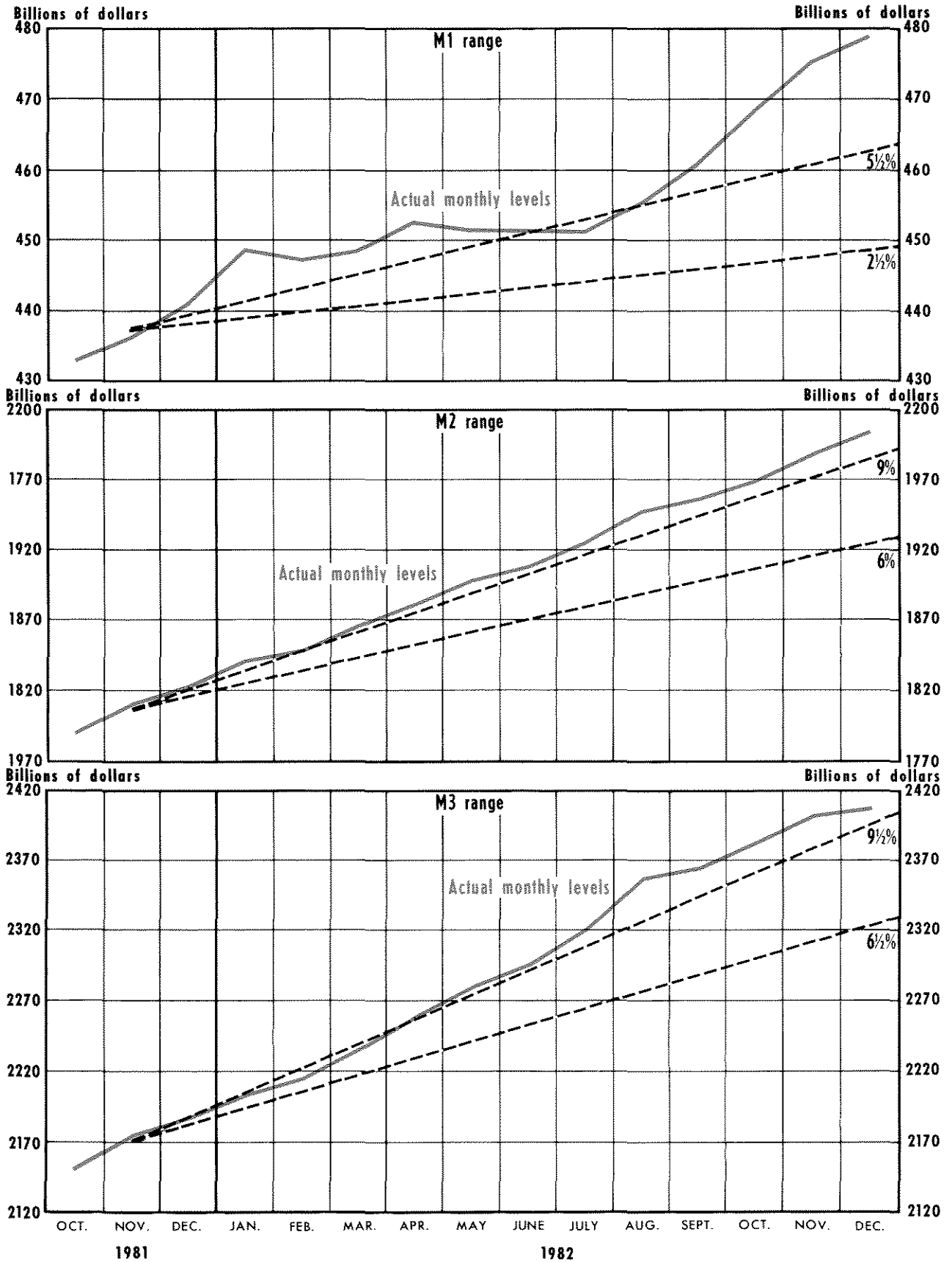
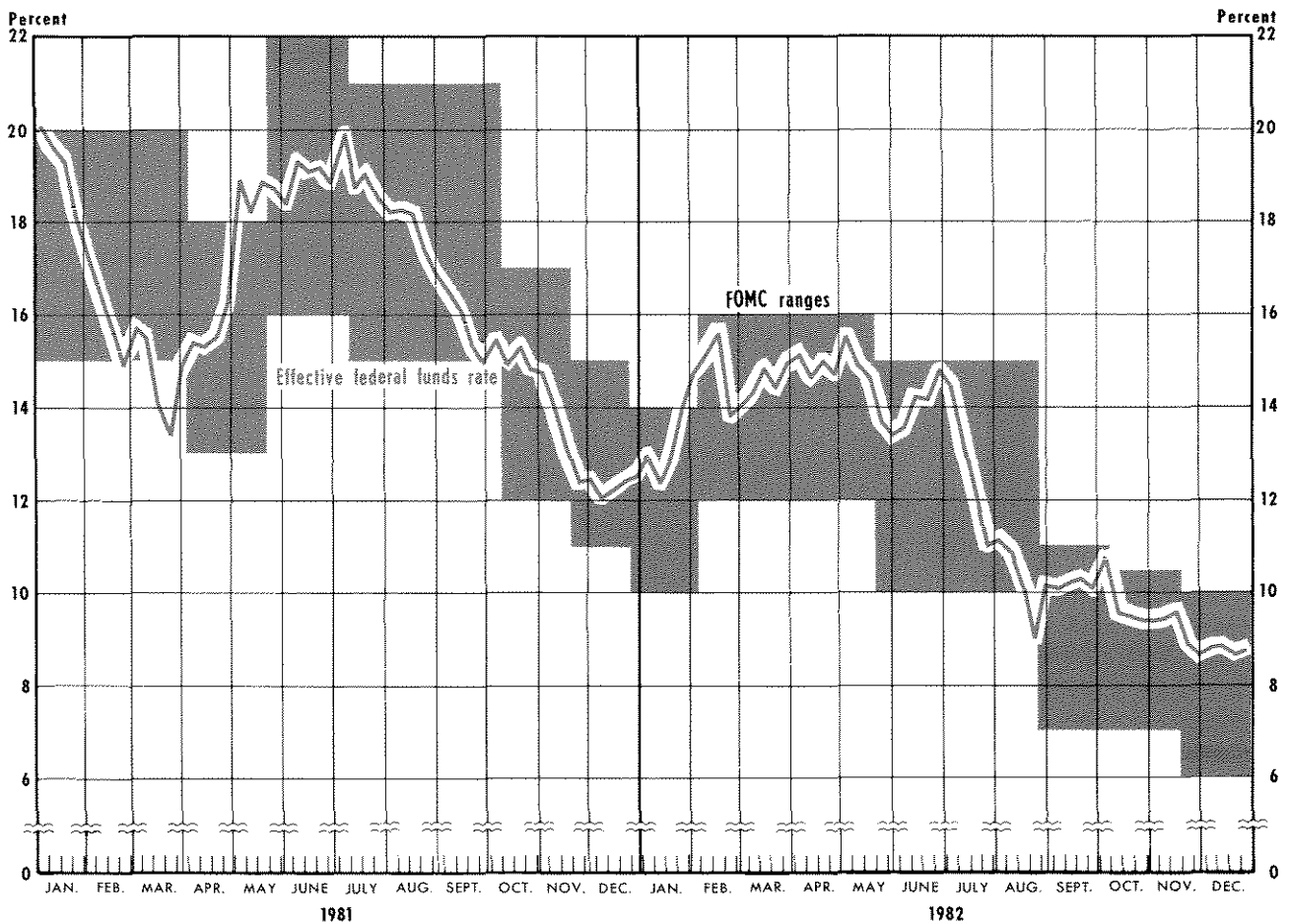


Chart 2

FOMC Ranges for Federal Funds Rate



NOTE: Rates are calculated as weekly averages of daily rates. At each meeting the committee specified a range for the federal funds rate. These ranges are indicated for the first full week they were in effect.

relative weight that should be given to M1 and M2 in implementing the Committee's short-run policy decisions.¹¹ Indeed, the relative importance of M2 and M1 for short-run policy purposes shifted during the year.

Nevertheless, just as in 1981, short-run movements in the aggregates during 1982 followed their short-run target paths. This correspondence between the target paths and actual growth of the aggregates is illustrated in chart 3, which shows the short-run target ranges and actual levels of M1 and M2, respectively, based on first-published data. First-published data give a more

accurate representation of the Committee's short-run policy decisions based on information available at the time.¹² Chart 3 shows that short-run targets for M1 were specified only for the first three quarters of the year. During its October meeting, the Committee decided to place much less weight than usual on the narrow aggregate and not set a specific objective for its growth. At this time, the Committee began setting short-run targets for M3.

First Quarter

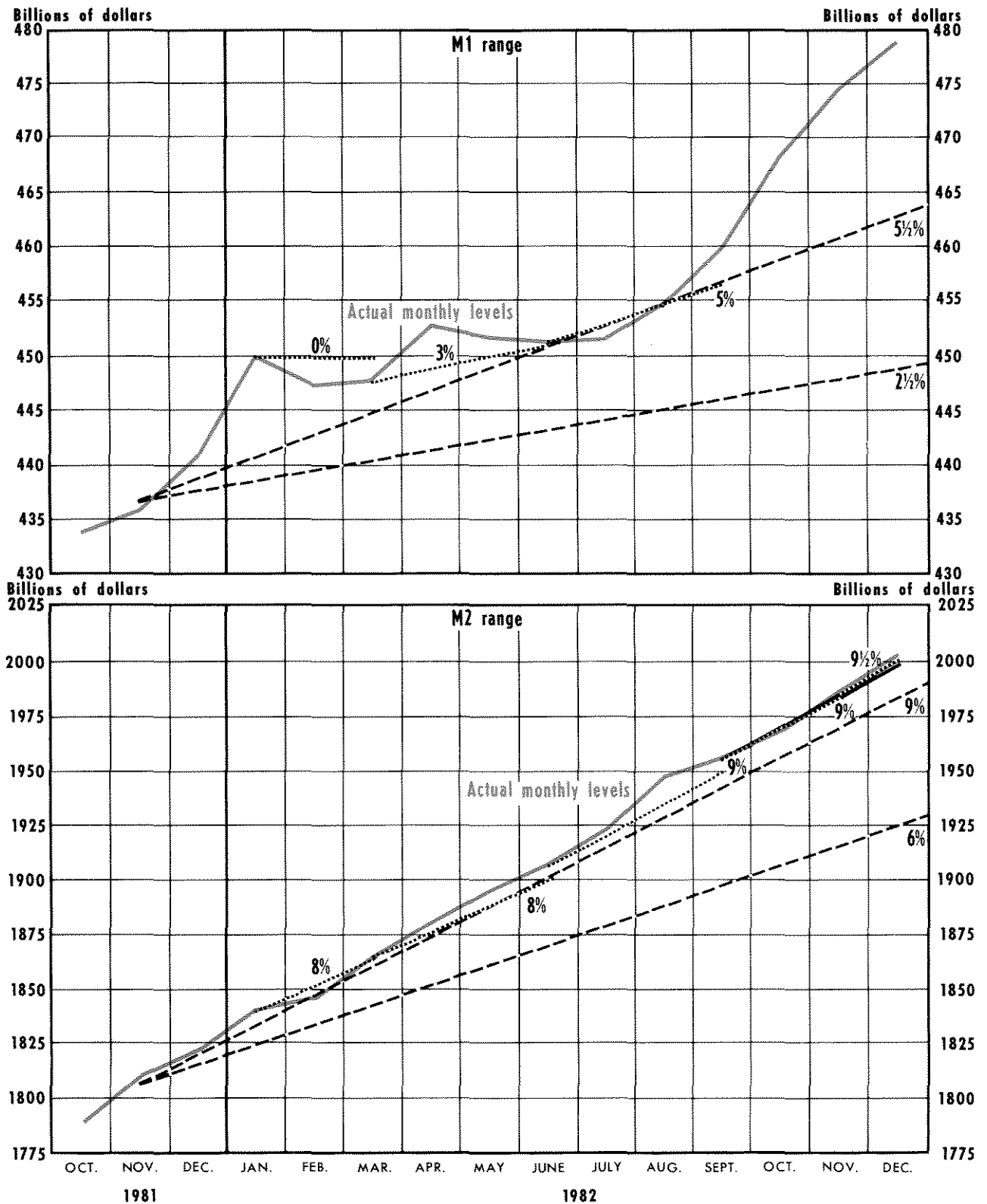
The short-run targets for the first quarter of 1982 were made against a backdrop of rapid expansion in M2 and M1 from November 1981. The growth of both monetary aggregates accelerated during January 1982, especially that of M1. The Committee believed that the rapid growth in the demand for components of M1 would abate during the ensuing months. It noted that if

¹¹See Daniel L. Thornton, "The FOMC in 1981: Monetary Control in a Changing Financial Environment," this *Review* (April 1982), pp. 3-22.

¹²Because of a definitional change, data for M2 prior to February 5, 1982, are not first-published. Prior to that date, M2 included repurchase agreements and institution-only money market mutual funds.

Chart 3

Short-Term and Long-Term Growth Objectives Based on First Published Data



NOTE: Long dashed lines represent the long-term growth objective for the period IV/81-IV/82. Short dashed lines represent the current short-term growth objectives. Data, except for M2 published before 2/5/82, are first published from the Board's H-6 release. Prior to 2/5/82, M2 included RPs and institution-only MMMFs.

such a decline were not forthcoming, the income velocity of M1 would decline at a postwar record rate, based on the then-projected growth of nominal GNP for the first quarter. Thus, the Committee established growth paths for M1 and M2 that, if achieved, would move these aggregates closer to the upper limit of their annual target ranges. Specifically, the Committee sought no further growth in M1 from January to March and growth of M2 at an annual rate of around 8 percent. It was agreed that some decline in M1 would be acceptable in the context of reduced pressures in the money market.¹³

Second Quarter

Continued uncertainty about the relative behavior of M1 and M2 marked the short-run policy decisions for the second quarter. Staff analysis continued to suggest that the demand for money might be expected to moderate significantly in the second quarter. Furthermore, the Committee was concerned that technical problems associated with the federal income tax deadline in April might result in an April bulge in M1 growth. It was understood that most, if not all, of the M1 growth for the second quarter might occur during April.¹⁴

Given these technical factors and given uncertainties about near-term economic prospects and other factors affecting the monetary aggregates, most members of the Committee favored actions that would permit modest growth in M1 over the second quarter. Thus, the Committee set a short-run target for M1 of about 3 percent, while maintaining the short-run target growth rate for M2 at its first-quarter rate. Furthermore, it noted that deviations from these targets should be evaluated in the light that M2 was less likely than M1 to be affected by deposit shifts and technical factors over the second quarter.¹⁵

Third Quarter

In setting its short-run objectives for the third quarter, the Committee noted that the growth of M1 and

M2 for the whole period from March to June appeared to be in line with its objectives for that period (see chart 3). The Committee was increasingly pessimistic, however, about the outlook for the economy, and it continued to be concerned about the uncertainty over the public's demand for liquidity and precautionary balances. Additionally, it was concerned that the midyear reduction in withholding rates for federal income taxes and the scheduled cost-of-living increase in social security payments would lead to a bulge in M1 during July. After a discussion of these factors, most of the Committee members agreed that they would accept somewhat faster monetary growth in the third quarter if the demand for liquidity and precautionary balances did not ease as anticipated. Thus, the Committee voted for faster growth for both M1 and M2 from the second to the third quarter, increasing the M1 target from about 3 percent to about 5 percent and increasing the M2 target from about 8 percent to about 10 percent.¹⁶

De-emphasizing M1

At the October meeting, when the short-run objectives for the fourth quarter were first considered, a number of new considerations concerning the state of the economy and financial markets emerged. The Committee was concerned that the general worsening of the world economy and financial problems associated with large accumulated external debts of developing countries in recent years had contributed to an atmosphere of uncertainty that was reflected in the exchange value of the dollar, among other things. This in turn, had serious implications for U.S. export industries and for the ability of foreign governments to pursue flexible monetary policies. Also, the Committee was concerned that the U.S. banking system had been subjected to pressures associated with the general uneasiness about further credit problems both domestically and internationally. The result was a general widening of risk premiums, with interest rates on private securities generally falling less than the rates on Treasury issues from July to September. It noted that short-term interest rates had tended to move up in the weeks just before the meeting. Furthermore, the committee noted that the widely held expectations of a spring or summer recovery had been disappointed, and there were no signs of a strengthening in the economy.¹⁷

¹³See "Record" (April 1982), p. 234.

¹⁴See "Record" (June 1982), p. 368.

¹⁵The Committee reevaluated its position for the second quarter at its May meeting. Most members agreed that somewhat more rapid growth of M1 might be acceptable if it appeared to be associated with a continued desire of the public to build up liquidity, and if the growth of M2 was near its specified range. See "Record" (July 1982), p. 420.

¹⁶Three members dissented from this action because they favored a policy of bringing growth of M1 down to its range for 1982 by year-end. See table 1 or "Record" (September 1982), p. 548.

¹⁷See "Record" (December 1982), pp. 763-64.

With respect to the monetary aggregates, the Committee faced two new concerns: First, a large volume of all-savers certificates would mature in early October. Second, later in the quarter, the Depository Institution Deregulation Committee (DIDC) would implement the Garn-St Germain Depository Institutions Act of 1982 and create an account that would be equivalent to and competitive with money market mutual funds. While the exact nature of this new account and the timing of its implementation were unknown in October, it was known that the new account would be free of interest rate ceilings and would have some degree of usefulness for transaction purposes.¹⁸

It was believed that the maturing all-savers certificates would induce a temporary increase in M1, while the new money market deposit accounts (MMDAs) would depress M1 growth upon their introduction. Because of these conflicting effects, the Committee believed it would be difficult to interpret movements in M1 during the months ahead.¹⁹ It acknowledged that the new accounts also would affect the growth of M2; however, it believed that M2 and the broader aggregates would be affected to a much smaller extent than M1. Therefore, it decided to set no specific objectives for M1 growth for the fourth quarter, to increase the weight given to M2 and to set short-run policy objectives for M3.

At the November meeting, the Committee acknowledged that the bulge in M1 growth, which it had anticipated, had persisted longer than some members expected, but staff analysis suggested M1 growth could be expected to decelerate over the remainder of the fourth quarter. It was noted, however, that growth of both M1 and M2 could accelerate in the near term due to a buildup of balances for eventual placement in the new MMDAs.²⁰ The Committee concluded that some-

what slower growth in M2 for the fourth quarter would be desirable if such growth were associated with a decline in market interest rates, and that somewhat faster growth would be tolerated if exceptional liquidity demands persisted. Once again, the Committee decided not to set specific policy objectives for M1.

The growth of M2 during the fourth quarter was very near the Committee's short-run objective (see chart 3). The growth of M1, however, was extremely rapid, growing at an annual rate of nearly 14 percent. This rapid fourth-quarter growth of M1 resulted in a fourth-quarter-to-fourth-quarter growth rate of 8.5 percent, well above the upper end of the long-run target range for the year.

SUMMARY

As in 1981, the FOMC argued that a number of financial developments and innovations continued to make it difficult to interpret movements in the two principal monetary aggregates, M1 and M2, during 1982. From the beginning of the year, the Committee believed that M2 was less likely to be affected by these factors than M1. This opinion was bolstered by unusual declines in the income velocity of M1 during the first and fourth quarters of 1982. It was generally felt that considerable weight should be given to M2 in interpreting developments during the year. The Committee increased the weight given to M2 during the year, ultimately dropping M1 as an explicit intermediate policy target for the fourth quarter.

Nevertheless, the growth of both M1 and M2 followed the short-run growth objectives of the Committee fairly closely during the year. Growth of M1 was near the Committee's short-run path until the fourth quarter, when short-run growth objectives for the aggregate were dropped. Actual growth of M2 was near the Committee's desired short-run path for the entire year. Rapid fourth-quarter growth of M1, however, pushed its growth well above the Committee's long-run range.

¹⁸At the time of this meeting (October 5), the Act had not been enacted (October 15). The Act required implementation of the new account no later than 60 days after taking effect.

¹⁹There was, however, some reason to believe that the effect of the new money market deposit accounts (MMDAs) on M1 would be minimal. See John A. Tatom, "Money Market Deposit Accounts, Super-NOWs and Monetary Policy," this *Review* (March 1983), pp. 5-16.

²⁰By this time, the Committee knew that MMDAs would become effective on December 14, 1982. See "Record" (January 1983), p. 19.

